

Fair Taxes ★ Quality Schools



A COMMONWEALTH OF OPPORTUNITY PLAN

A Budget and Tax Reform Plan

Creating Tax Fairness

Keeping our Commitment to Education

Preserving Virginia's Fiscal Integrity

Fiscally Responsible Approach

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The Warner Administration has instituted sweeping reforms to help ensure accountability to taxpayers and restore Virginia's fiscal stability. We have worked with the General Assembly to close a \$6 billion budget shortfall:

- Eliminated more than 50 agencies, boards, and commissions.
- Eliminated 5,000 positions from state government.
- Cut every agency by an average of 20%.
- Produced significant savings through government-wide efficiency plans.

But more must be done.

A Long-Term Vision

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To sustain our progress, Governor Warner has proposed a tax and budget reform plan with three goals.

1. Make the tax system more fair.
2. Meet Virginia's Constitutional commitment to education.
3. Protect the Commonwealth's fiscal integrity.

Creating Tax Fairness: *What the Plan Will Accomplish*

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- ✓ Lower the income tax for most Virginians.
- ✓ Reduce the food tax by 1.5 cents and add 1 cent to the sales tax.
- ✓ Close corporate loopholes.
- ✓ Increase Virginia's lowest-in-nation state cigarette tax to pay for health care needs. Give counties ability to levy the tax, up to a cap.
- ✓ Finish the promise to end the car tax.
- ✓ Eliminate estate tax for working farms and family-owned businesses.
- ✓ End the unfair accelerated sales tax collection for retailers.
- ✓ Provide incentives for small and mid-size businesses to invest.
- ✓ Ease the tax burden on military, reservists, and National Guard families.
- ✓ Streamline collection of the state sales tax.

Creating Tax Fairness: *Individual Income Tax*

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- ✓ Provide a larger personal exemption (from \$800 to \$1,000).
- ✓ Provide a larger standard deduction for individuals (from \$3,000 to \$4,000).
- ✓ Eliminate the marriage penalty (raising the standard deduction for married couples from \$5,000 to \$8,000).
- ✓ Lower income taxes for all filers on first \$20,000 income.
- ✓ Raise the income threshold for filing tax returns (from \$5,000 to \$7,000 for individuals and from \$8,000 to \$14,000 for couples).
- ✓ Conform to provisions of the federal Military Family Relief Act.
- ✓ Create 6.25% bracket for those with taxable income above \$100,000. *Less than 8% of filers are affected.*

Creating Tax Fairness: *Reforming Age Deduction*

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- ✓ Preserve \$12,000 deduction for current seniors 65 and older.
- ✓ Preserve \$6,000 deduction for current seniors aged 62 – 64.
- ✓ For persons turning 65 after January 1, 2005, the age deduction will be based on income.
 - For individuals, the age deduction will be reduced by \$1 for every \$2 above \$50,000 of income, and phased out for individuals with incomes above \$74,000.
 - For couples, the age deduction will be reduced by \$1 for every \$2 above \$75,000 of income, and phased out for couples with incomes above \$123,000.
 - The \$6,000 deduction for persons aged 62 to 64 will no longer be available for those who become 62 after January 1, 2005.

100% of Current Seniors 65 and Older are Unaffected.

Over 75% Of Future Single and Married Seniors

Will Not Be Affected.

Creating Tax Fairness: *Sales and Use Tax*

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- ✓ Lower sales tax on groceries (from 4 cents to 2.5 cents by 2005) (1 cent reduction on July 1, 2004; additional half cent reduction on July 1, 2005)
- ✓ Increase sales tax on non-food items by one cent (currently 2nd lowest sales tax in nation). Virginia remains lower than most neighboring states.
- ✓ End unfair accelerated sales tax filing for retailers adopted in 2002 as one-time budget fix.
- ✓ Modernize the state sales tax by adopting the multi-state streamlined sales tax statute (without sourcing rules), effective July 1, 2006. (This will not allow taxes on internet access.)

Creating Tax Fairness: *Car Tax*

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Eliminate car tax (frozen currently at 70%) in budgets proposed during Governor Warner's term, subject to existing triggers:

✓ 77.5% in 2005.

✓ 85% in 2006.

✓ 92.5% in 2007.

✓ 100% elimination in 2008.

Creating Tax Fairness: *Cigarette Tax*

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- ✓ 2.5 cents per pack state tax moves to 25 cents per pack, dedicated for health care.
- ✓ Expand taxing authority to counties over three years, and cap combined state and local taxes at 75 cents per pack (50 cpp local, 25 cpp state).
 - July 1, 2004 up to 20 cpp
 - July 1, 2005 up to a total of 35 cpp
 - July 1, 2006 up to a total of 50 cpp
- ✓ Localities that have a higher local cigarette tax than 50 cpp may levy their existing tax, but may not raise it further.

Ease the pressure on local property taxes.

Creating Tax Fairness: *Estate, Business, & Corporate Income*

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- ✓ Fully eliminate estate tax on working farms and closely held businesses (if they comprise the majority of the estate), and estates up to \$10 million in value.
- ✓ Stimulate investment by allowing companies to deduct as business expenses up to \$100,000 in equipment purchases (conform to recent federal tax changes).
- ✓ Close corporate tax loopholes. *21 of 50 largest corporate employers paid no corporate income tax in Virginia in 1999.*
 - Eliminate “Delaware holding company” loophole.
 - Eliminate “nowhere income,” ensuring that profits on goods shipped from Virginia are taxed in Virginia, unless they are taxed in another state.
 - Require more “pass-through entities” to identify their owners, most of whom live outside Virginia.

Keeping our Commitments

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The budget and tax reform plan enables Virginia to:

- ✓ Properly fund the Standards of Quality (SOQ) for public education (enrollment growth, inflation, and teacher retirement estimated at an additional \$774 million).
- ✓ Begin to address chronic underfunding of higher education (increase investment by \$144 million over biennium to address enrollment and research needs).
- ✓ Keep commitment to transportation by dedicating part of the insurance premiums tax and paying debt service on FRANs from the general fund (additional \$392 million over biennium).
- ✓ Begin to replenish the Revenue Stabilization Fund.
- ✓ Make Virginia financially stable and reduce pressure on local governments to raise property taxes.

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A Simplified Look at the State's Two-Year Budget

General Fund (\$27.0 billion – 46%)

Income Tax
Corporate Income Tax
Sales Tax
Insurance Premiums Taxes
Utility Taxes

Pays for:

Public Schools
Colleges and Universities
State Police and Prisons
Medicaid (state match)
Mental Health Programs
Car Tax Relief
Economic Development Grants
Public Health Programs
General Government Operations

Nongeneral Fund (\$32.0 billion – 54%)

Federal Funds.....
Tuition and Fees.....
Transportation Revenue (gas tax, etc).....
Patient Revenues.....
Unemployment Payroll Taxes.....
Child Support Enforcement Collections.....
ABC and Lottery Operations.....
Permit Fees.....
Bond Proceeds.....

Pays for:

Education, Research, Welfare, and Medicaid
Colleges and Universities (including dorms & dining halls)
Roads, Airports, Ports, Mass Transit
Mental Hospitals, UVa Hospital, MCV
Unemployment Compensation
Child Support
State Enterprises
Safety and Health Inspections and Business Regulation
Capital Projects

Preserving Virginia's Fiscal Integrity

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Why can't we meet basic commitments within the current revenue structure?

Fiscal Reality: Virginia still faces a substantial budget shortfall next biennium -- without any new programs.

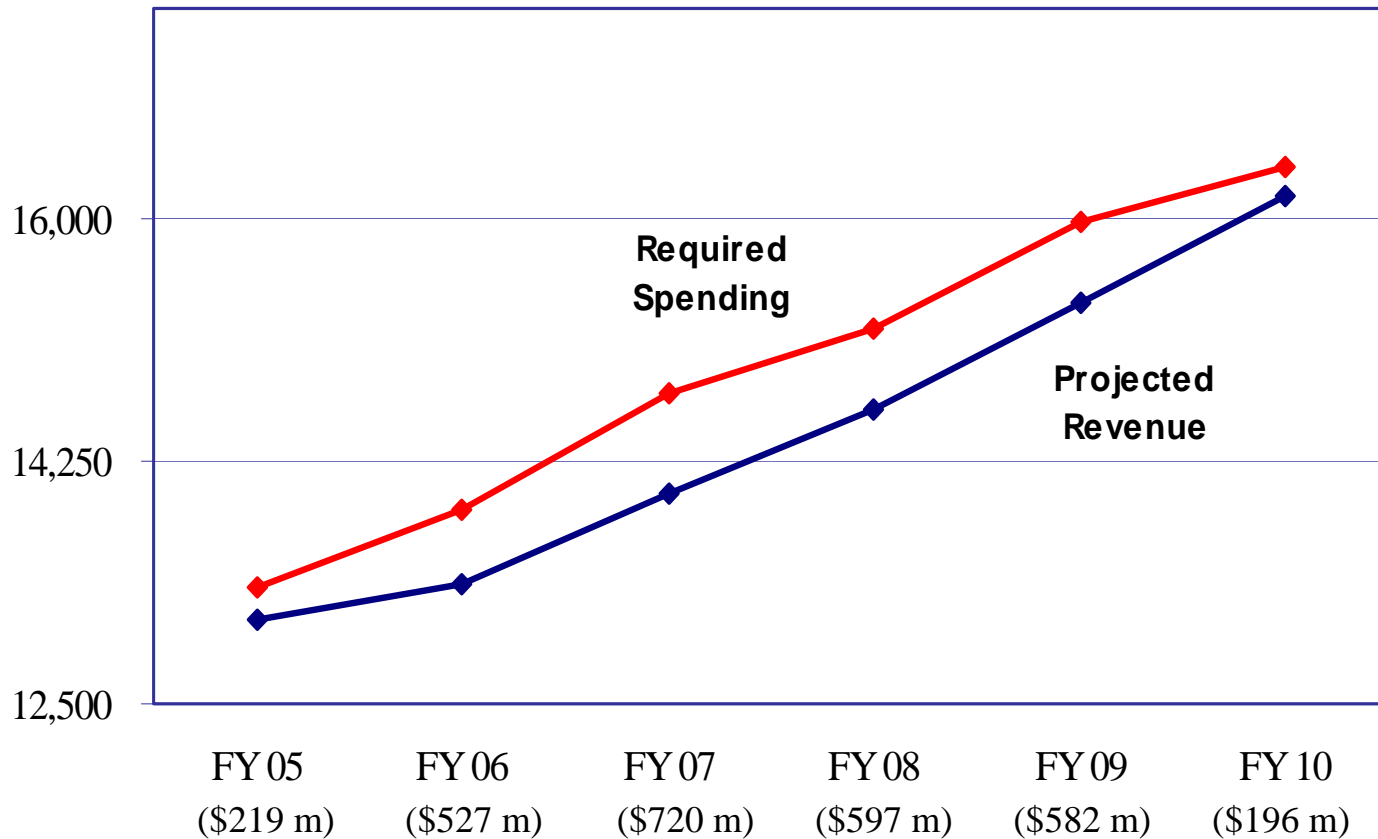
- Medicaid: Baseline growth above 8% per year means \$800 million in additional costs for health care needs.
- Adult Inmates: More than 4% a year average growth in adult inmates in this decade exceeds prison capacity.
- Public Education: 100,000 new students by end of decade and commitment to pay the state share of the Standards of Quality.
- Car Tax Cut: Growth in vehicles and value of cars means \$160 million above current costs in the next biennium, even at 70% reimbursement.
- Transportation: Aging roadways mean that over \$400 million in construction funding has to be used for ordinary maintenance in this 6-year plan.
- Continuing effect of absorbing the fiscal impact of the 50 different tax breaks granted since 1995, many of which grow over time.

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Required Spending Exceeds Projected Revenue Through the End of the Decade

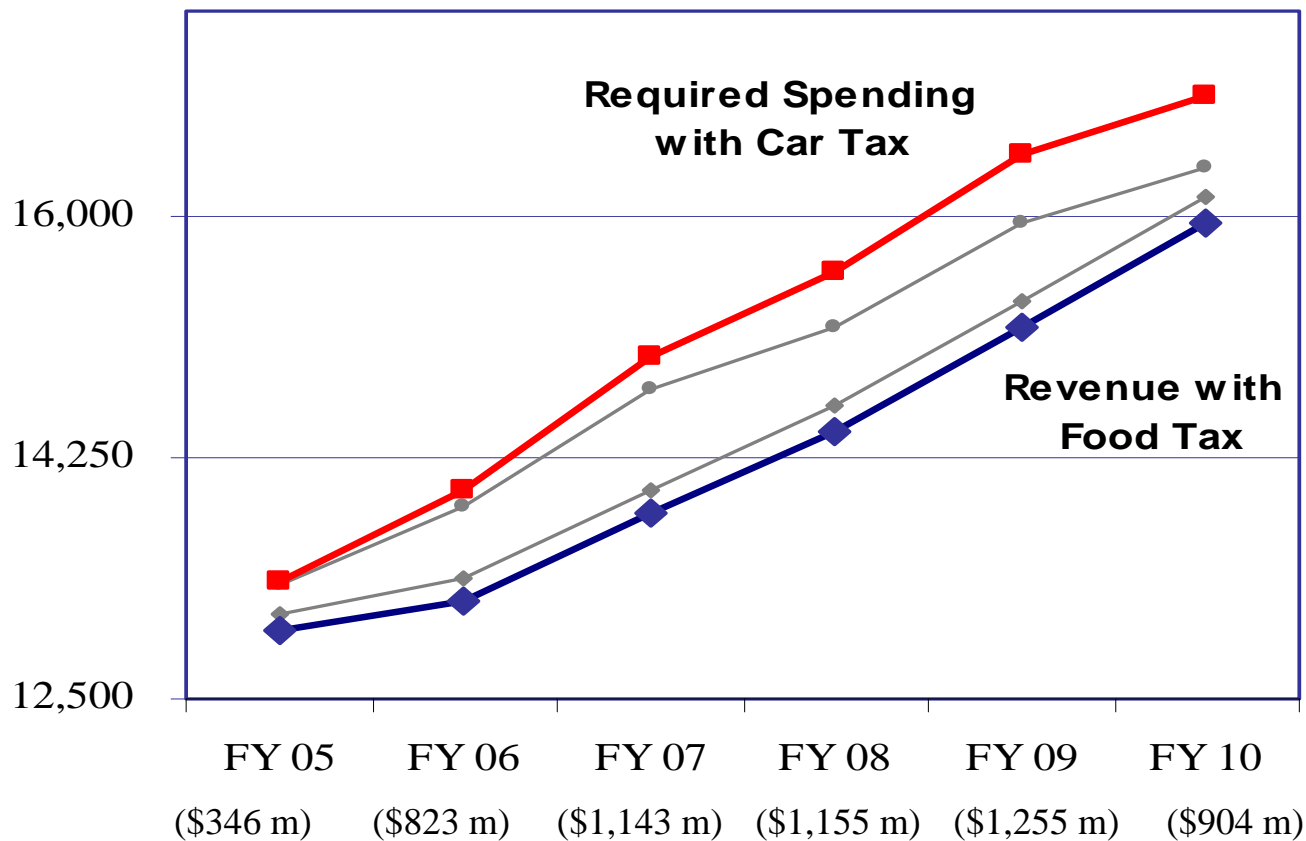
(in millions of dollars)



Preserving Virginia's Fiscal Integrity

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With Car Tax at 100% and Food Tax Relief, the Budget Shortfalls Worsen



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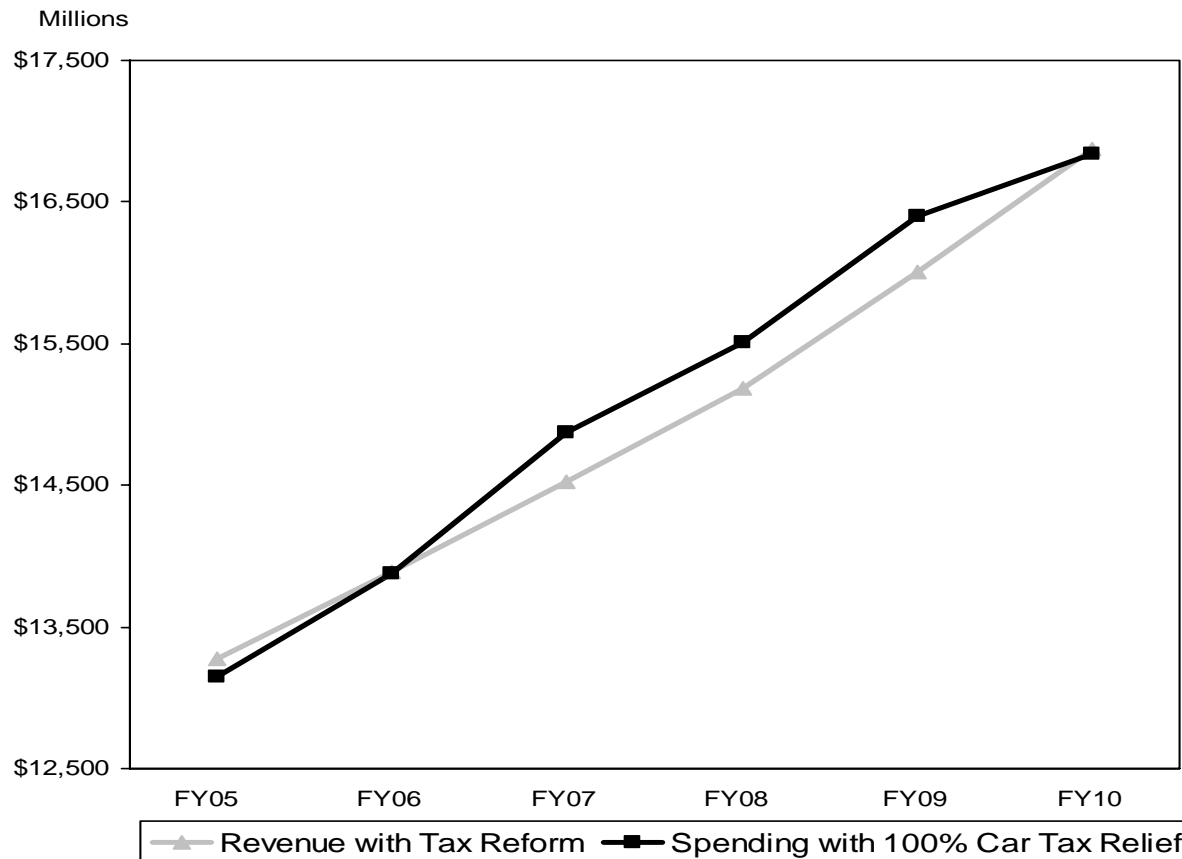
The Commonwealth of Opportunity budget and tax reform plan will:

- ✓ Make the tax code fair: 65% pay less.
- ✓ Meet Virginia's basic obligations:
 - FY 04: –\$10.3 million
 - FY 05: +\$481.6 million
 - FY 06: +\$546.2 million in new revenue
- ✓ Create no new programs or entitlements.
- ✓ Allow replenishment of the Revenue Stabilization Fund.
- ✓ Help preserve our coveted AAA bond rating.
- ✓ Return Virginia to responsible budget practices.

Preserving Virginia's Fiscal Integrity

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The Budget and Tax Reform Plan restores stability, but keeps the pressure on for future savings . . .



Creating Tax Fairness

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**A plan that's fair to the
people who pay the bills.**

65%

pay less